



## STATE BOARD OF EQUALIZATION STAFF LEGISLATIVE BILL ANALYSIS

Date Amended	<b>06/14/99</b>	Bill No:	<b>AB 601</b>
Tax:	<b>Property</b>	Author:	<b>Cedillo et al.</b>
Board Position:		Related Bills:	

### **BILL SUMMARY:**

This bill would, in part, create “Urban Adaptive Reuse Zones” within which individual buildings designated by local governments would be valued according to a special capitalization of income method.

### **ANALYSIS:**

#### Current Law:

Under current law, there are no special provisions to assess commercial buildings located in economically depressed areas that are converted to residential use. Existing law provides preferential assessment treatment for certain historical properties. Article XIII, Section 8 provides that “[t]o promote the preservation of property of historical significance, the Legislature may define such property and shall provide that when it is enforceably restricted, in a manner specified by the Legislature, it shall be valued for property tax purposes only on a basis that is consistent with its restrictions and uses.”

Revenue and Taxation Code Section 402.1 provides that in the assessment of land, the assessor shall consider the effect upon value of any enforceable restrictions to which the use of the land may be subjected, including a restriction as a result of a recorded contract with a governmental agency.

#### Proposed Law:

This bill would authorize a new type of economic development area, called an urban adaptive reuse zone (UARZ). The Trade and Commerce Agency (TCA) would be required to designate up to 10 UARZs from applications submitted by local governing bodies. The designations would be binding for ten years with the possibility of a ten-year extension if specified vacancy rates exist at the end of the ten-year initial designation period.

Local legislative bodies may by ordinance designate buildings located within the UARZ as “qualified adaptive reuse buildings.” To be designated, buildings must have been built before 1975 and have been 50% or more vacant, excluding first floor retail space, for a period of six months or longer. Qualified adaptive reuse buildings includes (1) conversion of a nonresidential building to include at least 25% of the floor area as residential units or 50% of the floor area as live-work units, or (2) a 50% increase in residential or live-work use of floor area of an existing residential or live-work building. The property owner must

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sign an agreement to use the property for adaptive reuse housing for 10-years. At the option of the property owners, the restriction agreement may be renewed for up to an additional 10 years, if the adaptive reuse housing remains.

With respect to property taxes, this bill would extend the special assessment provisions for valuing enforceably restricted historical properties to qualified adaptive reuse buildings located in urban adaptive reuse zones. When valuing a qualified adaptive reuse building, the property would be valued by the capitalization of annual income method set forth in the statute. Section 439.2 is explicit in its instructions as to the estimation of the income to be capitalized and the rate used to capitalize the income. (Assessment procedures pursuant to Section 439.2 are more favorable than those provided for under Section 402.1).

In General:

**Historical Properties.** Owners of certain historical or architecturally significant properties may benefit from limitations placed on the assessor's valuation. The property must be on the National Register of Historic Places or in a historic district. If not, the property can still qualify if it is listed on the official register of the state, a county, or a city as a historic or architecturally significant site, place, or landmark. The owner must enter into a contract with a city or county that provides for the preservation of the property for a specified period of time. The contract may also call for the owner to restore or rehabilitate the property in conformance with the rules and regulations of the Office of Historic Preservation of the Department of Parks and Recreation, with the contract binding on any successor to the owner.

**COMMENTS:**

1. **Sponsor and Purpose.** This bill is sponsored by Central City Association of Los Angeles in an effort to create an incentive program for the adaptive reuse of older, mostly vacant commercial buildings in those California cities where this activity is not yet market driven.
2. **This bill would extend the existing assessment procedures for enforceably restricted historical properties to qualifying commercial buildings built prior to 1975 that are planned to be converted to residential uses.** These properties would be valued at the lowest of three values: 1) the restricted income method, 2) the Proposition 13 value (factored base year value) or 3) current fair market value.
3. **Responsibility for determining whether a specific building located within a zone would qualify for these special assessment provisions would rest with the local agency entering into the agreement.** The owner of a building would be required to sign an agreement with the local governing agency to use the property for adaptive reuse housing for a period of ten years.

4. **Suggested Amendments.** As drafted, this bill appears to require the assessor to monitor whether the property is being used according to the terms and conditions of the agreement entered into by the property owner and the local governing body. That duty *This staff analysis is provided to address various administrative, cost, revenue and policy issues; it is not to be construed to reflect or suggest the Board's formal position.*

is more appropriately placed on the local agency who entered into the agreement. The following suggested amendment to Section 439.2 would clarify this point:

439.2 (g) If the owner of a property subject to an adaptive reuse restriction agreement, as described in Section 7093 of the Government Code, fails to operate the property in accordance with the terms and conditions of the agreement, the local legislative body that entered into the agreement shall notify the county assessor who shall reassess the property without regard to the methods provided in this section and shall add a penalty equal to 120 percent of the cumulative tax relief received under this section.

### **COST ESTIMATE:**

The costs associated with this measure are absorbable.

### **REVENUE ESTIMATE:**

#### **Proposal**

This bill would authorize a new type of economic development area called Urban Adaptive Reuse Zone (UARZ). The California Trade and Commerce Agency would designate up to ten UARZs statewide. Buildings located within a UARZ and designated by the local legislative body as “qualified adaptive reuse buildings” would be assessed by the capitalization of income method that is currently used when valuing enforceably restricted historical property.

#### **Background, Methodology, and Assumptions**

Urban Adaptive Reuse Zones would be active for 10 years with the possibility of a 5-year extension if the vacancy rate among commercial buildings constructed prior to 1975 within the UARZ is 20 percent or higher at the end of the initial 10-year period. Buildings eligible for qualified adaptive reuse are those buildings built before 1975 that have been at least 50 percent vacant, excluding first floor retail space, for a period of six months or longer. Qualified adaptive reuse includes (1) conversion of a nonresidential building to include at least 25 percent of the floor area as residential units or 50 percent of the floor area as live/work units, or (2) a 50 percent increase in residential or live/work use of floor area of an existing residential or live/work building. Any difference in property tax revenue would only result from the difference in assessed value using the capitalization of income method above compared to the assessed value under other valuation methods, including Proposition 13 or Proposition 8.

The revenue effect cannot be estimated due to the multiple factors involved and the lack of data for any of these factors. These factors include:

1. The size and location of the Urban Adaptive Reuse Zones cannot be predicted.

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2. Since counties do not report the distribution of their rolls by year of construction, we have no estimate of the percentage of commercial properties built before 1975.
3. Current and future vacancy rates cannot be determined.
4. Since current and future rental rates are not available, the difference in assessed value using the capitalization of income method compared to the current assessed value cannot be determined.

### Revenue Summary

Because this bill involves several unknown and unpredictable variables, in particular the size and scope of the zones and projects involved, it is not possible to determine the potential revenue decrease. However, it is possible the potential growth of these projects could escalate into much larger revenue losses in future years.

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